Activities of Principal Subsidiaries

Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S") in the United States, acts as a broker (i.e., agent) for corporate, institutional, government, and other clients and as a dealer (i.e., principal) in the purchase and sale of corporate securities. MLPF&S also acts as a broker and/or a dealer in the purchase and sale of mutual funds, money market instruments, government securities, high yield bonds, municipal securities, financial futures contracts and options. The futures business and foreign exchange activities are conducted through MLPF&S and other subsidiaries. MLPF&S holds memberships and/or has third-party clearing relationships with all major commodity and financial futures exchanges and clearing associations in the United States and it also carries positions reflecting trades executed on exchanges outside of the United States through affiliates and/or third-party clearing brokers. As a leading investment banking entity, MLPF&S provides corporate, institutional, and government clients with a wide variety of financial services including underwriting the sale of securities to the public, structured and derivative financing, private placements, mortgage and lease financing and financial advisory services, including advice on mergers and acquisitions.

MLPF&S also provides securities clearing services for its own account and for unaffiliated broker-dealers through its *Broadcort Correspondent Clearing Division* and through its subsidiary Merrill Lynch Professional Clearing Corp. ("ML Pro"). ML Pro is involved in our prime brokerage business and also makes a market in listed option contracts on various options exchanges.

MLPF&S also provides discretionary and non-discretionary investment advisory services. These advisory services include Merrill Lynch Consults® Service, the Personal Investment Advisory Program, the Merrill Lynch Mutual Fund Advisor® program, the Merrill Lynch Mutual Fund Advisor Selects® program, Merrill Lynch Personal Advisor program, and Merrill Lynch Global Selects. MLPF&S also offers fee-based financial planning services, including the Financial Foundation® report. MLPF&S provides financing to clients, including margin lending and other extensions of credit. Through the *Beyond Banking*® account, our customers have access to a special securities account product designed for everyday transactions, savings and cash management that combines Visa, check writing and ATM access with available advice and guidance. We also offer Merrill Lynch branded credit cards.

Through its retirement group, MLPF&S provides a wide variety of investment and custodial services to individuals through Individual Retirement Accounts and small business retirement programs. MLPF&S also provides investment, administration, communications, and consulting services to corporations and their employees for their retirement programs, including 401(k), pension, profit-sharing and non-qualified deferred compensation plans.

Merrill Lynch International ("MLI") is a United Kingdom-based dealer in equity and fixed income securities of a significant number of global issuers, sovereign government obligations and asset-backed securities, and in loans and related financial instruments. Outside the United States, MLI is a registered market maker and regularly makes a market in the equity securities of the more actively traded non-U.S. corporations. MLI is also our primary non-U.S. credit and equity derivatives and futures product dealer.

Merrill Lynch Government Securities, Inc. ("MLGSI") is a primary dealer in obligations issued or guaranteed by the U.S. Government and regularly makes a market in securities issued by Federal agencies and other government-sponsored entities, such as, among others, Government National Mortgage Association, Fannie Mae and Freddie Mac. MLGSI deals in mortgage-backed pass-through instruments issued by certain of these entities and also in related futures, options, and forward contracts for its own account, to hedge its own risk, and to facilitate customers' transactions. As a primary dealer, MLGSI acts as a counterparty to the Federal Reserve Bank of New York ("FRBNY") in the conduct of open market operations and regularly reports positions and activities to the FRBNY. An integral part of MLGSI's business involves entering into repurchase agreements and securities lending transactions.

Merrill Lynch Capital Services, Inc. ("MLCS") and Merrill Lynch Derivative Products AG ("MLDP") are Merrill Lynch's primary interest rate and currency derivative product dealers. MLCS primarily acts as a counterparty for certain derivative financial products, including interest rate and currency swaps, caps and floors and options. MLCS maintains positions in interest-bearing securities, financial futures and forward contracts to hedge its interest rate and currency risk related to derivative exposures. In the normal course of its business, MLCS enters into repurchase and resale agreements with certain affiliated companies. MLDP acts as an intermediary for certain derivative products, including interest rate and currency swaps, between MLCS and counterparties that are highly rated or otherwise acceptable to MLDP. Its activities address certain swap customers' preference to limit their trading to those dealers having the highest credit quality. MLDP has been assigned the Aaa, AAA and AAA counterparty rating by the rating agencies Moody's Investors Service, Standard & Poor's Ratings Services and Fitch Ratings, respectively. Customers meeting certain credit criteria enter into swaps with MLDP and, in turn, MLDP enters into offsetting mirror swaps with MLCS. However, MLCS is required to provide MLDP with collateral to mitigate certain exposures MLDP may have to MLCS. In addition, MLCS's subsidiaries, Merrill Lynch Commodities, Inc., Merrill Lynch Commodities (Europe) Trading Limited and other Merrill Lynch subsidiaries trade as principal in physically and financially settled contracts in energy, weather and a broad range of other commodities. These subsidiaries also provide asset optimization and other energy management and risk management services for third parties.

Merrill Lynch Bank USA ("MLBUSA") and Merrill Lynch Bank & Trust Co., FSB ("MLBT-FSB") are part of the Merrill Lynch Global Bank Group, which provides the management platform for Merrill Lynch's banking products and services. In July 2006, Merrill Lynch Trust Company, FSB ("MLTC-FSB") received approval from the Office of Thrift Supervision ("OTS") to become a full service thrift institution as part of an internal reorganization of certain banking businesses of Merrill Lynch. On August 5, 2006, Merrill Lynch Bank & Trust Co. ("MLB&T"), an existing Federal Deposit Insurance Corporation ("FDIC")-insured depository institution, was merged into MLTC-FSB, and MLTC-FSB was renamed Merrill Lynch Bank & Trust Co., FSB.

Merrill Lynch, primarily through MLBUSA, provides syndicated and bridge financing, asset-based lending, commercial real estate lending, equipment financing, and standby or "backstop" credit in various forms for large institutional clients generally in connection with their commercial paper programs. MLBUSA also offers securities-based loans primarily to individual clients. MLBUSA is a state-chartered depository institution whose deposits are insured by the FDIC, and is a wholesale bank for Community Reinvestment Act ("CRA") purposes. MLBT-FSB is an FDIC-insured federal savings bank and is a retail bank for CRA purposes. MLBUSA and MLBT-FSB offer certificates of deposit, transaction accounts and money market deposit accounts and issue Visa® debit cards.

MLBT-FSB, through its subsidiary Merrill Lynch Credit Corporation, offers residential mortgage financing throughout the United States enabling clients to purchase and refinance their homes as well as to manage their other personal credit needs. In addition, Merrill Lynch Business Financial Services Inc. ("MLBFS"), a subsidiary of MLBUSA, engages in commercial financing for qualifying small- and middle-market businesses, including lines of credit, revolving loans, term loans and equipment leases and loans. MLBFS provides qualifying business clients with acquisition, working capital and equipment financing, commercial real estate financing, and other specialized asset financing.

Financial Data Services Inc., a wholly-owned subsidiary of MLBUSA, is a registered transfer agent and provides support and services for mutual fund products.

Merrill Lynch International Bank Limited ("MLIB"), formerly known as Merrill Lynch Capital Markets Bank Limited, is the primary non-U.S. banking entity for Merrill Lynch. Headquartered in Ireland, with branch offices in Amsterdam, Bahrain, Frankfurt, London, Madrid, Milan and Singapore, MLIB acts as a principal for debt derivative transactions and engages in advisory, lending, loan trading, and institutional sales activities. MLIB also provides collateralized (including mortgage) lending, letters of credit, guarantees and foreign exchange services to, and accepts deposits from, its clients.

MLIB, through its subsidiaries, Mortgages plc and Freedom Funding Limited, provides mortgage lending, administration and servicing in the U.K. nonconforming residential mortgage market.

Merrill Lynch Bank (Suisse) S.A., a subsidiary of MLIB, is a Swiss licensed bank that provides a full array of banking, asset management and brokerage products and services to international clients, including securities trading and custody, secured loans and overdrafts, fiduciary deposits, foreign exchange trading and portfolio management services.

On September 30, 2006, Merrill Lynch completed an internal reorganization of its non-U.S. banking structure, when the entire business of mlib (historic) (the UK entity previously known as Merrill Lynch International Bank Limited) was transferred to MLIB after obtaining all necessary regulatory approvals and pursuant to High Court Orders granted in London and Singapore. The two entities were renamed as part of this reorganization. Following the transfer, mlib (historic) ceased to conduct business activity.

Merrill Lynch Mortgage Capital Inc. ("MLMCI") is a dealer in syndicated commercial loans. As an integral part of its business, MLMCI enters into repurchase agreements whereby it obtains funds by pledging its own whole loans as collateral. The repurchase agreements provide financing for MLMCI's inventory and serve as short-term investments for MLMCI's customers. MLMCI also enters into reverse repurchase agreements through which it provides funds to customers collateralized by whole loan mortgages, thereby providing the customers with temporary liquidity. MLMCI, through its subsidiary Merrill Lynch Mortgage Lending, Inc. ("MLML"), is a dealer in whole loan mortgages, mortgage loan participations, mortgage loan servicing and a commercial mortgage conduit that makes, and purchases from lenders, both commercial and multi-family mortgage loans and then securitizes these loans for sale to investors. MLML purchases prime, subprime, nonperforming and subperforming residential mortgage loans from originators of these loans and aggregates these loans for sale in the securitization market. Wilshire Credit Corporation, a subsidiary of MLMCI, services subprime, nonperforming and reperforming residential mortgages.

Merrill Lynch Japan Securities Co., Ltd. ("MLJS") is a Japan-based broker-dealer that provides clients with a variety of financial services, including the purchase and sale of equity and fixed income securities, futures and options. MLJS also acts as an underwriter and seller of securities in both publicly registered transactions and private placements.

Merrill Lynch Life Insurance Company and ML Life Insurance Company of New York issue annuity products. The sale of non-proprietary insurance products and proprietary and non-proprietary annuity products are made through Merrill Lynch Life Agency Inc. and other affiliated insurance agencies operating in the United States.

ML IBK Positions, Inc. is a U.S.-based entity involved in private equity and principal investing that makes proprietary investments in all levels of the capital structure of U.S. and non-U.S. companies, and in special purpose companies owning real estate, mortgage loans, consumer receivables and other assets, and may make direct equity investments in real estate assets, mortgage loans and other assets. In addition, through its subsidiary, Merrill Lynch Capital Corporation, it provides senior and subordinated financing to certain companies.

Management's Discussion of Financial Responsibility, Disclosure Controls and Procedures, and Report on Internal Control Over Financial Reporting

Financial Responsibility

Oversight is provided by independent units within Merrill Lynch, working together to maintain Merrill Lynch's internal control standards. Corporate Audit reports directly to the Audit Committee of the Board of Directors, providing independent appraisals of Merrill Lynch's internal controls and compliance with established policies and procedures. Finance management establishes accounting policies and procedures, measures and monitors financial risk, and independently from the businesses prepares financial statements that fairly present the underlying transactions and events of Merrill Lynch. Independent risk groups monitor capital adequacy and liquidity management and have oversight responsibility for Merrill Lynch's market and credit risks independent from business line management. These groups have clear authority to enforce trading and credit limits using various systems and procedures to monitor positions and risks. The Office of the General Counsel serves in a counseling and advisory role to management and the business groups. In this role, the Office of the General Counsel develops policies; works with the business in monitoring compliance with internal policies, external rules, and industry regulations; and provides legal advice, representation, execution, and transaction support to the businesses.

ML & Co. has established a Disclosure Committee to assist the Chief Executive Officer and Chief Financial Officer in fulfilling their responsibilities for overseeing the accuracy and timeliness of disclosures made by ML & Co. The Disclosure Committee is made up of senior representatives of Merrill Lynch's Finance, Investor Relations, Office of the General Counsel, Treasury, Tax and independent risk groups, and is responsible for implementing and evaluating disclosure controls and procedures on an ongoing basis. The Disclosure Committee meets at least eight times a year. Meetings are held as needed to review key events and disclosures impacting the period throughout each fiscal quarter and prior to the filing of ML & Co.'s Form 10-K and 10-Q reports and proxy statement with the SEC.

The Board of Directors designated Merrill Lynch's Guidelines for Business Conduct as the Company's code of ethics for directors, officers and employees in performing their duties. The Guidelines set forth written standards for employee conduct with respect to conflicts of interest, disclosure obligations, compliance with applicable laws and rules and other matters. The Guidelines also set forth information and procedures for employees to report ethical or accounting concerns, misconduct or violations of the Guidelines in a confidential manner. The Board of Directors adopted Merrill Lynch's Code of Ethics for Financial Professionals in 2003. The Code, which applies to all Merrill Lynch professionals who participate in our public disclosure process, supplements our Guidelines for Business Conduct and is designed to promote honest and ethical conduct, full, fair and accurate disclosure and compliance with applicable laws.

The independent registered public accounting firm, Deloitte & Touche LLP, performs annual audits of Merrill Lynch's financial statements in accordance with the Standards of the Public Company Accounting Oversight Board (United States). They openly discuss with the Audit Committee their views on the quality of the financial statements and related disclosures and the adequacy of Merrill Lynch's internal accounting controls. Quarterly review reports on the unaudited interim financial statements are also issued by Deloitte & Touche LLP. The Audit Committee appoints the independent registered public accounting firm. The independent registered public accounting firm is given unrestricted access to all financial records and related data, including minutes of meetings of stockholders, the Board of Directors, and committees of the Board.

As part of their oversight role, committees of the Board supervise management in the formulation of corporate policies, procedures and controls. The Audit Committee, which consists of five independent directors, oversees Merrill Lynch's system of internal accounting controls and the internal audit function. In addition, the Audit Committee oversees the development and implementation of risk management and compliance policies, procedures, and functions. It also reviews the annual Consolidated Financial Statements with management and Merrill Lynch's independent registered public accounting firm, and evaluates the performance, independence and fees of our independent registered public accounting firm and the professional services it provides. The Audit Committee also has the sole authority to appoint or replace the independent registered public accounting firm.

The Finance Committee, which consists of four independent directors, reviews, recommends, and approves policies regarding financial commitments and other expenditures. It also reviews and approves certain financial commitments, acquisitions, divestitures, and proprietary investments. In addition, the Finance Committee oversees balance sheet and capital management, corporate funding policies and financing plans. It also reviews Merrill Lynch's policies and procedures for managing exposure to market and credit risks.

Disclosure Controls and Procedures

ML & Co.'s Disclosure Committee assists with implementing, monitoring and evaluating our disclosure controls and procedures. ML & Co.'s Chief Executive Officer, Chief Financial Officer and Disclosure Committee have evaluated the effectiveness of ML & Co.'s disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Report. Based on that evaluation, ML & Co.'s Chief Executive Officer and Chief Financial Officer have concluded that ML & Co.'s disclosure controls and procedures are effective.

In addition, no change in ML & Co.'s internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934) occurred during the fourth fiscal quarter of 2006 that has materially affected, or is reasonably likely to materially affect, ML & Co.'s internal control over financial reporting.

Report on Internal Control Over Financial Reporting

Management recognizes its responsibility for establishing and maintaining adequate internal control over financial reporting and has designed internal controls and procedures to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements and related notes in accordance with generally accepted accounting principles in the United States of America. Management assessed the effectiveness of Merrill Lynch's internal control over financial reporting as of December 29, 2006. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control-Integrated Framework*. Based on our assessment, management believes that Merrill Lynch maintained effective internal control over financial reporting as of December 29, 2006.

Deloitte & Touche LLP, Merrill Lynch's independent registered public accounting firm, has issued an attestation report on management's assessment of Merrill Lynch's internal control over financial reporting and on the effectiveness of Merrill Lynch's internal control over financial reporting. This report appears under *"Report of Independent Registered Public Accounting Firm"* on the following page.

New York, New York
February 26, 2007

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of Merrill Lynch & Co., Inc.:

We have audited management's assessment, included in the accompanying Report on Internal Control Over Financial Reporting, that Merrill Lynch & Co., Inc. and subsidiaries ("Merrill Lynch") maintained effective internal control over financial reporting as of December 29, 2006, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Merrill Lynch's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of Merrill Lynch's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Merrill Lynch maintained effective internal control over financial reporting as of December 29, 2006, is fairly stated, in all material respects, based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, Merrill Lynch maintained, in all material respects, effective internal control over financial reporting as of December 29, 2006, based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 29, 2006 of Merrill Lynch and our report dated February 26, 2007 expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the change in accounting method in 2006 for share-based payments to conform to Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment.*

Deloitte + Touche LLP

New York, New York
February 26, 2007

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of Merrill Lynch & Co., Inc.:

We have audited the accompanying consolidated balance sheets of Merrill Lynch & Co., Inc. and subsidiaries ("Merrill Lynch") as of December 29, 2006 and December 30, 2005, and the related consolidated statements of earnings, changes in stockholders' equity, comprehensive income and cash flows for each of the three years in the period ended December 29, 2006. These financial statements are the responsibility of Merrill Lynch's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Merrill Lynch as of December 29, 2006 and December 30, 2005, and the results of its operations and its cash flows for each of the three years in the period ended December 29, 2006, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, in 2006 Merrill Lynch changed its method of accounting for share-based payments to conform to Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment*.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Merrill Lynch's internal control over financial reporting as of December 29, 2006, based on the criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 26, 2007 expressed an unqualified opinion on management's assessment of the effectiveness of Merrill Lynch's internal control over financial reporting and an unqualified opinion on the effectiveness of Merrill Lynch's internal control over financial reporting.

Deloitte + Touche LLP

New York, New York
February 26, 2007

Consolidated Statements of Earnings

(dollars in millions, except per share amounts)	Year Ended Last Friday in December 2006 (52 weeks)	2005 (52 weeks)	2004 (53 weeks)
Net Revenues			
Principal transactions	$ 7,034	$ 3,545	$ 2,197
Managed accounts and other fee-based revenues	6,539	6,031	5,440
Commissions	5,952	5,219	4,720
Investment banking	4,680	3,797	3,473
Revenues from consolidated investments	570	438	346
Other	3,259	2,195	1,454
	28,034	21,225	17,630
Interest and dividend revenues	40,588	26,571	14,989
Less interest expense	35,932	21,774	10,560
Net interest profit	4,656	4,797	4,429
Gain on merger	1,969	–	–
Total Net Revenues	34,659	26,022	22,059
Non-Interest Expenses			
Compensation and benefits	17,003	12,441	10,663
Communications and technology	1,844	1,608	1,461
Brokerage, clearing, and exchange fees	1,097	856	773
Occupancy and related depreciation	998	938	893
Professional fees	884	727	715
Advertising and market development	692	599	533
Expenses of consolidated investments	380	258	231
Office supplies and postage	226	210	203
Other	1,109	1,154	751
Total Non-Interest Expenses	24,233	18,791	16,223
Earnings Before Income Taxes	10,426	7,231	5,836
Income Tax Expense	2,927	2,115	1,400
Net Earnings	$ 7,499	$ 5,116	$ 4,436
Preferred Stock Dividends	188	70	41
Net Earnings Applicable to Common Stockholders	$ 7,311	$ 5,046	$ 4,395
Earnings Per Common Share			
Basic	$ 8.42	$ 5.66	$ 4.81
Diluted	$ 7.59	$ 5.16	$ 4.38
Dividends Paid Per Common Share	$ 1.00	$ 0.76	$ 0.64
Average Shares Used in Computing Earnings Per Common Share			
Basic	868.1	890.7	912.9
Diluted	963.0	977.7	1,003.8

See Notes to Consolidated Financial Statements.

Consolidated Balance Sheets

(dollars in millions, except per share amounts)	Dec. 29, 2006	Dec. 30, 2005
Assets		
Cash and cash equivalents	**$ 32,109**	$ 14,586
Cash and securities segregated for regulatory purposes or deposited with clearing organizations	**13,449**	11,949
Securities financing transactions		
Receivables under resale agreements	**178,368**	163,021
Receivables under securities borrowed transactions	**118,610**	92,484
	296,978	255,505
Trading assets, at fair value *(includes securities pledged as collateral that can be sold or repledged of $58,966 in 2006 and $31,471 in 2005)*		
Equities and convertible debentures	**48,527**	32,933
Mortgages, mortgage-backed, and asset-backed	**44,588**	29,233
Corporate debt and preferred stock	**32,854**	27,436
Contractual agreements	**31,913**	26,216
Non-U.S. governments and agencies	**21,075**	15,157
U.S. Government and agencies	**13,086**	8,936
Municipals and money markets	**7,243**	5,694
Commodities and related contracts	**4,562**	3,105
	203,848	148,710
Investment securities	**83,410**	69,273
Securities received as collateral	**24,929**	16,808
Other receivables		
Customers *(net of allowance for doubtful accounts of $41 in 2006 and $46 in 2005)*	**49,427**	40,451
Brokers and dealers	**18,900**	12,127
Interest and other	**21,054**	15,619
	89,381	68,197
Loans, notes, and mortgages *(net of allowance for loan losses of $478 in 2006 and $406 in 2005)*	**73,029**	66,041
Separate accounts assets	**12,314**	16,185
Equipment and facilities *(net of accumulated depreciation and amortization of $5,213 in 2006 and $4,865 in 2005)*	**2,924**	2,313
Goodwill and other intangible assets	**2,457**	6,035
Other assets	**6,471**	5,413
Total Assets	**$ 841,299**	$ 681,015

Consolidated Balance Sheets

(dollars in millions, except per share amounts)	Dec. 29, 2006	Dec. 30, 2005
Liabilities		
Securities financing transactions		
Payables under repurchase agreements	$ 222,624	$ 193,067
Payables under securities loaned transactions	43,492	19,335
	266,116	212,402
Short-term borrowings	18,110	8,987
Deposits	84,124	80,016
Trading liabilities, at fair value		
Contractual agreements	38,311	28,755
Equities and convertible debentures	23,268	19,119
Non-U.S. governments and agencies	13,385	19,217
U.S. Government and agencies	12,510	12,478
Corporate debt and preferred stock	6,323	6,203
Commodities and related contracts	3,606	2,029
Municipals, money markets and other	1,459	1,132
	98,862	88,933
Obligation to return securities received as collateral	24,929	16,808
Other payables		
Customers	49,414	35,619
Brokers and dealers	24,282	19,528
Interest and other	36,096	28,501
	109,792	83,648
Liabilities of insurance subsidiaries	2,801	2,935
Separate accounts liabilities	12,314	16,185
Long-term borrowings	181,400	132,409
Junior subordinated notes (related to trust preferred securities)	3,813	3,092
Total Liabilities	802,261	645,415
Commitments and Contingencies		
Stockholders' Equity		
Preferred Stockholders' Equity *(liquidation preference of $30,000 per share; issued: 2006 — 105,000 shares; 2005 — 93,000 shares)*	3,145	2,673
Common Stockholders' Equity		
Shares exchangeable into common stock	39	41
Common stock *(par value $1.33 1/3 per share; authorized: 3,000,000,000 shares; issued: 2006 —1,215,381,006 shares and 2005 — 1,148,714,008 shares)*	1,620	1,531
Paid-in capital	18,919	13,320
Accumulated other comprehensive loss (net of tax)	(784)	(844)
Retained earnings	33,217	26,824
	53,011	40,872
Less: Treasury stock, at cost *(2006 — 350,697,271 shares; 2005 — 233,112,271 shares)*	17,118	7,945
Total Common Stockholders' Equity	35,893	32,927
Total Stockholders' Equity	39,038	35,600
Total Liabilities and Stockholders' Equity	$ 841,299	$ 681,015

See Notes to Consolidated Financial Statements.

Consolidated Statements of Changes in Stockholders' Equity

	Year Ended Last Friday in December					
	Amounts			Shares		
(dollars in millions)	**2006**	2005	2004	**2006**	2005	2004
Preferred Stock, net						
Balance, beginning of year	**$ 2,673**	$ 630	$ 425	**89,685**	21,000	42,500
Issuances	**374**	2,143	630	**12,000**	72,000	21,000
Redemptions	**–**	–	(425)	**–**	–	(42,500)
Shares (repurchased) re-issuances	**98**	(100)	–	**3,243**	(3,315)	–
Balance, end of year	**3,145**	2,673	630	**104,928**	89,685	21,000
Common Stockholders' Equity						
Shares Exchangeable into Common Stock						
Balance, beginning of year	**41**	41	43	**2,707,797**	2,782,712	2,899,923
Exchanges	**(2)**	–	(2)	**(47,871)**	(74,915)	(117,211)
Balance, end of year	**39**	41	41	**2,659,926**	2,707,797	2,782,712
Common Stock						
Balance, beginning of year	**1,531**	1,465	1,417	**1,148,714,008**	1,098,991,806	1,063,205,274
Shares issued to employees	**89**	66	48	**66,666,998**	49,722,202	35,786,532
Balance, end of year	**1,620**	1,531	1,465	**1,215,381,006**	1,148,714,008	1,098,991,806
Paid-in Capital						
Balance, beginning of year	**13,320**	11,460	10,053			
Employee stock plan activity	**2,351**	1,173	891			
Amortization of employee stock grants	**3,248**	687	516			
Balance, end of year	**18,919**	13,320	11,460			
Accumulated Other Comprehensive Loss						
Foreign Currency Translation Adjustment (net of tax)						
Balance, beginning of year	**(507)**	(289)	(301)			
Translation adjustment	**77**	(218)	12			
Balance, end of year	**(430)**	(507)	(289)			
Net Unrealized Gains (Losses) on Investment Securities Available-for-Sale Securities (net of tax)						
Balance, beginning of year	**(181)**	(91)	(111)			
Net unrealized gains (losses) on available-for-sale	**(15)**	(156)	30			
Other adjustments(1)	**4**	66	(10)			
Balance, end of year	**(192)**	(181)	(91)			
Deferred Gains (losses) on Cash Flow Hedges (net of tax)						
Balance, beginning of year	**(3)**	21	11			
Net deferred gains on cash flow hedges	**5**	(24)	10			
Balance, end of year	**2**	(3)	21			
Defined benefit pension and postretirement plans (net of tax)						
Balance, beginning of year	**(153)**	(122)	(150)			
Minimum pension liability adjustment	**(76)**	(31)	28			
Adjustment to initially apply SFAS 158(2)	**65**	–	–			
Balance, end of year	**(164)**	(153)	(122)			
Balance, end of year	**(784)**	(844)	(481)			
Retained Earnings						
Balance, beginning of year	**26,824**	22,485	18,692			
Net earnings	**7,499**	5,116	4,436			
Preferred stock dividends declared	**(188)**	(70)	(41)			
Common stock dividends declared	**(918)**	(707)	(602)			
Balance, end of year	**33,217**	26,824	22,485			
Treasury Stock, at cost						
Balance, beginning of year	**(7,945)**	(4,230)	(1,195)	**(233,112,271)**	(170,955,057)	(117,294,392)
Shares repurchased	**(9,088)**	(3,700)	(2,968)	**(116,610,876)**	(63,068,200)	(54,029,600)
Shares issued to (reacquired from) employees(3)	**(89)**	(18)	(74)	**(1,021,995)**	836,071	251,724
Share exchanges	**4**	3	7	**47,871**	74,915	117,211
Balance, end of year	**(17,118)**	(7,945)	(4,230)	**(350,697,271)**	(233,112,271)	(170,955,057)
Total Common Stockholders' Equity	**35,893**	32,927	30,740			
Total Stockholders' Equity	**$ 39,038**	$ 35,600	$ 31,370			

(1) Other adjustments relate to policyholder liabilities, deferred policy acquisition costs, and income taxes.

(2) For the initial year of application, the adjustment is not reflected on the Statement of Comprehensive Income.

(3) Share amounts are net of reacquisitions from employees of 6,622,887 shares, 4,360,607 shares and 4,982,481 shares in 2006, 2005 and 2004, respectively.

See Notes to Consolidated Financial Statements

Consolidated Statements of Comprehensive Income

(dollars in millions)	2006	Year Ended Last Friday in December 2005	2004
Net Earnings	**$ 7,499**	$ 5,116	$ 4,436
Other Comprehensive Income (Loss)			
Foreign currency translation adjustment:			
Foreign currency translation gains (losses)	**(366)**	129	(359)
Income tax (expense) benefit	**443**	(347)	371
Total	**77**	(218)	12
Net unrealized gains (losses) on investment securities available-for-sale:			
Net unrealized holding gains (losses) arising during the period	**(16)**	184	365
Reclassification adjustment for realized (gains) losses included in net earnings	**1**	(340)	(335)
Net unrealized gains (losses) on investment securities available-for-sale	**(15)**	(156)	30
Adjustments for:			
Policyholder liabilities	**1**	12	19
Deferred policy acquisition costs	**–**	(2)	–
Income tax (expense) benefit	**3**	56	(29)
Total	**(11)**	(90)	20
Deferred gains (losses) on cash flow hedges:			
Deferred gains (losses) on cash flow hedges	**9**	(2)	(7)
Reclassification adjustment for realized losses (gains) included in net earnings	**(2)**	(23)	10
Income tax (expense) benefit	**(2)**	1	7
Total	**5**	(24)	10
Defined benefit pension and postretirement plans:			
Minimum pension liability adjustment	**(110)**	(46)	38
Income tax (expense) benefit	**34**	15	(10)
Total	**(76)**	(31)	28
Total Other Comprehensive Income (Loss)	**(5)**	(363)	70
Comprehensive Income	**$ 7,494**	$ 4,753	$ 4,506

See Notes to Consolidated Financial Statements

Consolidated Statements of Cash Flows

(dollars in millions)	Year Ended Last Friday in December 2006	2005	2004
Cash flows from operating activities			
Net earnings	**$ 7,499**	$ 5,116	$ 4,436
Non-cash items included in earnings:			
Gain on merger	**(1,969)**	–	–
Depreciation and amortization	**523**	473	506
Share-based compensation expense	**3,156**	1,003	876
Deferred taxes	**(360)**	232	2
Policyholder reserves	**123**	129	144
Undistributed earnings from equity investments	**(421)**	(417)	(400)
Other	**922**	888	23
Changes in operating assets and liabilities:			
Trading assets	**(55,392)**	25,902	(46,918)
Cash and securities segregated for regulatory purposes or deposited with clearing organizations	**(1,019)**	3,259	(5,466)
Receivables under resale agreements	**(15,346)**	(84,166)	(17,835)
Receivables under securities borrowed transactions	**(26,126)**	2,014	(38,426)
Customer receivables	**(9,562)**	(2,217)	(7,041)
Brokers and dealers receivables	**(6,825)**	(19)	(4,768)
Proceeds from loans, notes, and mortgages held for sale	**41,317**	31,255	29,399
Other changes in loans, notes, and mortgages held for sale	**(47,670)**	(34,554)	(30,731)
Trading liabilities	**(6,097)**	(17,007)	14,447
Payables under repurchase agreements	**29,557**	44,386	58,846
Payables under securities loaned transactions	**24,157**	(2,901)	11,155
Customer payables	**13,795**	1,238	12,141
Brokers and dealers payables	**4,791**	(605)	1,024
Other, net	**5,533**	(2,889)	2,962
Cash used for operating activities	**(39,414)**	(28,880)	(15,624)
Cash flows from investing activities			
Proceeds from (payments for):			
Maturities of available-for-sale securities	**13,222**	25,452	26,602
Sales of available-for-sale securities	**16,176**	36,574	27,983
Purchases of available-for-sale securities	**(31,357)**	(51,283)	(54,498)
Sales and maturities of held-to-maturity securities	**18**	16	37
Purchases of held-to-maturity securities	**(15)**	–	(4)
Loans, notes, and mortgages held for investment	**(681)**	(9,678)	(902)
Transfer of cash balances related to merger	**(651)**	–	–
Other investments and other assets	**(6,546)**	(1,442)	(1,854)
Equipment and facilities, net	**(1,174)**	(278)	(402)
Cash used for investing activities	**(11,008)**	(639)	(3,038)
Cash flows from financing activities			
Proceeds from (payments for):			
Short-term borrowings	**9,123**	(154)	(1,670)
Deposits	**4,108**	270	289
Issuance and resale of long-term borrowings	**87,814**	49,703	50,535
Settlement and repurchase of long-term borrowings	**(42,545)**	(31,195)	(23,231)
Derivative financing transactions	**16,259**	6,347	6,642
Issuance of common stock	**1,838**	858	589
Issuance of preferred stock, net	**472**	2,043	205
Common stock repurchases	**(9,088)**	(3,700)	(2,968)
Other common stock transactions	**539**	(80)	41
Excess tax benefits related to stock-based compensation	**531**	–	–
Dividends	**(1,106)**	(777)	(643)
Cash provided by financing activities	**67,945**	23,315	29,789
Increase (decrease) in cash and cash equivalents	**17,523**	(6,204)	11,127
Cash and cash equivalents, beginning of year	**14,586**	20,790	9,663
Cash and cash equivalents, end of year	**$ 32,109**	$ 14,586	$ 20,790
Supplemental disclosure of cash flow information:			
Cash paid for:			
Income taxes	**$ 2,638**	$ 1,443	$ 661
Interest	**35,685**	21,519	10,345

Non-cash investing and financing activities:

The investment recorded in connection with the merger of the MLIM business with BlackRock (See Note 2) totaled $7.7 billion. The book value of net asset transfers, derecognition of goodwill and other adjustments totaled $4.9 billion.

See Notes to Consolidated Financial Statements.

NOTE 1 Summary of Significant Accounting Policies

Description of Business

Merrill Lynch & Co., Inc. ("ML & Co.") and together with its subsidiaries, ("Merrill Lynch", "we", "our", or "us") provide investment, financing, insurance, and related services to individuals and institutions on a global basis through its broker, dealer, banking, insurance, and other financial services subsidiaries. Its principal subsidiaries include:

- Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S"), a U.S.-based broker-dealer in securities and futures commission merchant;
- Merrill Lynch International ("MLI"), a U.K.-based broker-dealer in securities and dealer in equity and credit derivatives;
- Merrill Lynch Government Securities Inc. ("MLGSI"), a U.S.-based dealer in U.S. Government securities;
- Merrill Lynch Capital Services, Inc., a U.S.-based dealer in interest rate, currency, credit derivatives and commodities;
- Merrill Lynch Bank USA ("MLBUSA"), a U.S.-based, state chartered, Federal Deposit Insurance Corporation ("FDIC")-insured depository institution;
- Merrill Lynch Bank & Trust Co., FSB ("MLBT-FSB"), a U.S.-based, federally chartered, FDIC-insured depository institution;
- Merrill Lynch International Bank Limited ("MLIB"), an Ireland-based bank;
- Merrill Lynch Mortgage Capital, Inc., a U.S.-based dealer in syndicated commercial loans;
- Merrill Lynch Japan Securities Co., Ltd. ("MLJS"), a Japan-based broker-dealer;
- Merrill Lynch Life Insurance Company ("MLLIC"), a U.S.-based provider of annuity products;
- ML Life Insurance Company of New York ("ML Life"), a U.S.-based provider of annuity products;
- Merrill Lynch Derivative Products, AG, a Switzerland-based derivatives dealer; and
- ML IBK Positions Inc., a U.S.-based entity involved in private equity and principal investing.

Services provided to clients by Merrill Lynch and other activities include:

- Securities brokerage, trading and underwriting;
- Investment banking, strategic advisory services (including mergers and acquisitions) and other corporate finance activities;
- Wealth management products and services, including financial, retirement and generational planning;
- Investment management and advisory and related record-keeping services;
- Origination, brokerage, dealer, and related activities in swaps, options, forwards, exchange-traded futures, other derivatives, commodities and foreign exchange products;
- Securities clearance, settlement financing services and prime brokerage;
- Private equity and other principal investing activities;
- Proprietary trading of securities, derivatives and loans;
- Banking, trust, and lending services, including deposit-taking, consumer and commercial lending, including mortgage loans, and related services;
- Insurance and annuities sales; and
- Research across the following disciplines: global fundamental equity research, global fixed income and equity-linked research, global economics and foreign exchange research and global investment strategy.

Basis of Presentation

The Consolidated Financial Statements include the accounts of Merrill Lynch and its subsidiaries. The Consolidated Financial Statements are presented in accordance with U.S. Generally Accepted Accounting Principles, which include industry practices. Intercompany transactions and balances have been eliminated.

The Consolidated Financial Statements are presented in U.S. dollars. Many non-U.S. subsidiaries have a functional currency (i.e., the currency in which activities are primarily conducted) that is other than the U.S. dollar, often the currency of the country in which a subsidiary is domiciled. Subsidiaries' assets and liabilities are translated to U.S. dollars at year-end exchange rates, while revenues and expenses are translated at average exchange rates during the year. Adjustments that result from translating amounts in a subsidiary's functional currency and related hedging, net of related tax effects, are reported in stockholders' equity as a component of accumulated other comprehensive loss. All other translation adjustments are included in earnings. Merrill Lynch uses derivatives to manage the currency exposure arising from activities in non-U.S. subsidiaries. See the Derivatives section for additional information on accounting for derivatives.

During the second quarter of 2006, Merrill Lynch began reporting cash flows from loans held for sale as operating activities, whereas in prior periods, these cash flows were classified as investing activities. Merrill Lynch corrected the previously presented cash flows for these loans to conform to U.S. Generally Accepted Accounting Principles. All prior period amounts have been restated to conform to this presentation.

During the fourth quarter of 2006, Merrill Lynch began reporting its master note program borrowings as secured short-term borrowings, whereas in prior periods, these borrowings were classified as payables under repurchase agreements. The impact on the December 30, 2005 balance sheet was $5.1 billion. In addition, Merrill Lynch has restated all prior period cash flows to conform to this presentation.

Merrill Lynch offers a broad array of products and services to its diverse client base of individuals, small to mid-size businesses, employee benefit plans, corporations, financial institutions, and governments around the world. These products and services are offered from a number of locations around the world. In some cases, the same or similar products and services may be offered to both individual and institutional clients, utilizing the same infrastructure. In other cases, a single infrastructure may be used to support multiple products and services offered to clients. When Merrill Lynch analyzes its profitability, it does not focus on the profitability of a single product or service. Instead, Merrill Lynch looks at the profitability of businesses offering an array of products and services to various types of clients. The profitability of the products and services offered to individuals, small to mid-size businesses, and employee benefit plans is analyzed separately from the profitability of products and services offered to corporations, financial institutions, and governments, regardless of whether there is commonality in products and services infrastructure. As such, Merrill Lynch does not separately disclose the costs associated with the products and services sold or general and administrative costs, in total or by product.

When pricing its various products and services, Merrill Lynch considers multiple factors, including prices being offered in the market for similar products and services, the competitiveness of its pricing compared to competitors, the profitability of its businesses and its overall profitability, as well as the profitability, creditworthiness, and importance of the overall client relationships.

Expenses which are incurred to support products and services and infrastructures shared by businesses are allocated to the businesses based on various methodologies which may include headcount, square footage, and certain other criteria. Similarly, certain revenues may be shared based upon agreed methodologies. When looking at the profitability of various businesses, Merrill Lynch considers all expenses incurred, including overhead and the costs of shared services, as all are considered integral to the operation of the businesses.

Consolidation Accounting Policies

The Consolidated Financial Statements include the accounts of Merrill Lynch, whose subsidiaries are generally controlled through a majority voting interest. In certain cases, Merrill Lynch subsidiaries may also be consolidated based on a risks and rewards approach. Merrill Lynch does not consolidate those special purpose entities that meet the criteria of a qualified special purpose entity ("QSPE").

Merrill Lynch determines whether it is required to consolidate an entity by first evaluating whether the entity qualifies as a voting rights entity ("VRE"), a variable interest entity ("VIE"), or a QSPE.

VREs — In accordance with the guidance in Financial Accounting Standards Board ("FASB") Interpretation No. 46, *Consolidation of Variable Interest Entities — an interpretation of ARB No. 51 ("FIN 46R")*, VREs consolidated by Merrill Lynch have both equity at risk that is sufficient to fund future operations and have equity investors with decision making ability that absorb the majority of the expected losses and expected returns of the entity. In accordance with Statement of Financial Accounting Standards ("SFAS") No. 94, *Consolidation of All Majority-Owned Subsidiaries ("SFAS No. 94")*, Merrill Lynch generally consolidates those VREs where it holds a controlling financial interest. For investments in limited partnerships and certain limited liability corporations that Merrill Lynch does not control, Merrill Lynch applies Emerging Issues Task Force Topic D-46, *Accounting for Limited Partnership Investments,* which requires use of the equity method of accounting for investors that have more than a minor influence, which is typically defined as an investment of greater than 3% of the outstanding equity in the entity. For more traditional corporate structures, Merrill Lynch applies the guidance in Accounting Principles Board Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock,* where Merrill Lynch has significant influence over the investee, which can be evidenced by a significant ownership interest (i.e., generally defined as ownership and voting interest of 20% to 50%), significant board of director representation, or other contracts and arrangements.

VIEs — Those entities that do not meet the criteria of a VRE as defined in FIN 46R are generally analyzed for consolidation as VIEs or QSPEs. Merrill Lynch consolidates those VIEs in which it absorbs the majority of the expected returns and/or the expected losses of the entity as required by FIN 46R. As discussed in the Use of Estimates section, Merrill Lynch relies on a quantitative and/or qualitative analysis, including an analysis of the purpose of the design of the entity, to determine whether it is the primary beneficiary of the VIE and therefore must consolidate the entity.

QSPEs — QSPEs are passive entities with significantly limited permitted activities. QSPEs are generally used as securitization vehicles and are limited in the type of assets they may hold, the derivatives that they can enter into and the level of discretion they may exercise through servicing activities. In accordance with SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities,* and FIN 46R, Merrill Lynch does not consolidate QSPEs.

Use of Estimates

In presenting the Consolidated Financial Statements, management makes estimates regarding:

- Valuations of assets and liabilities requiring fair value estimates including:
  - Trading inventory and investment securities;
  - Private equity and principal investments;
  - Loans and allowance for loan losses;
- The outcome of litigation;
- The realization of deferred taxes and tax reserves;
- Assumptions and cash flow projections used in determining whether VIEs should be consolidated and the determination of the qualifying status of special purpose entities;
- The carrying amount of goodwill and other intangible assets;
- The amortization period of intangible assets with definite lives;
- Valuation of share-based payment compensation arrangements;
- Insurance reserves and recovery of insurance deferred acquisition costs; and
- Other matters that affect the reported amounts and disclosure of contingencies in the financial statements.

Estimates, by their nature, are based on judgment and available information. Therefore, actual results could differ from those estimates and could have a material impact on the Consolidated Financial Statements, and it is possible that such changes could occur in the near term. A discussion of certain areas in which estimates are a significant component of the amounts reported in the Consolidated Financial Statements follows:

Trading Assets and Liabilities

Trading assets and liabilities are accounted for at fair value with realized and unrealized gains and losses reported in earnings. Fair values of trading securities are based on quoted market prices, pricing models (utilizing indicators of general market conditions and other economic measurements), or management's estimates of amounts to be realized on settlement, assuming current market conditions and an orderly disposition over a reasonable period of time. Estimating the fair value of certain illiquid securities requires significant management judgment. Merrill Lynch values trading security assets at the institutional bid price and recognizes bid-offer revenues when assets are sold. Trading security liabilities are valued at the institutional offer price and bid-offer revenues are recognized when the positions are closed.

Fair values for over-the-counter ("OTC") derivative financial instruments, principally forwards, options, and swaps, represent the present value of amounts estimated to be received from or paid to a third-party in settlement of these instruments. These derivatives are valued using pricing models based on the net present value of estimated future cash flows and directly observed prices from exchange-traded derivatives, other OTC trades, or external pricing services, while taking into account the counterparty's credit ratings, or Merrill Lynch's own credit ratings, as appropriate. Obtaining the fair value for OTC derivatives contracts requires the use of management judgment and estimates.

New and/or complex instruments may have immature or limited markets. As a result, the pricing models used for valuation often incorporate significant estimates and assumptions, which may impact the results of operations reported in the Consolidated Financial Statements. For long-dated and illiquid contracts, extrapolation methods are applied to observed market data in order to estimate inputs and assumptions that are not directly observable. This enables Merrill Lynch to mark-to-market all positions consistently when only a subset of prices are directly observable. Values for OTC derivatives are verified using observed information about the costs of hedging the risk and other trades in the market. As the markets for these products develop, Merrill Lynch continually refines its pricing models based on experience to correlate more closely to the market risk of these instruments. Unrealized gains at the inception of the derivative contract are not recognized unless the valuation model incorporates significant observable market inputs.

Valuation adjustments are an integral component of the fair valuation process and may be taken where either the sheer size of the trade or other specific features of the trade or particular market (such as counterparty credit quality or concentration or market liquidity) requires the valuation to be based on more than simple application of the pricing models.

Investment Securities

ML & Co. and certain of its non-broker-dealer subsidiaries follow the guidance prescribed by SFAS No. 115, *Accounting for Certain Investments in Debt and Equity Securities,* when accounting for investments in debt and publicly traded equity securities. Merrill Lynch classifies those debt securities that it has the intent and ability to hold to maturity as held-to-maturity securities, which are carried at cost unless a decline in value is deemed other-than-temporary, in which case the carrying value is reduced. Those securities that are bought and held principally for the purpose of selling them in the near term are classified as trading and marked to fair value through earnings. All other qualifying securities are classified as available-for-sale with unrealized gains and losses reported in accumulated other comprehensive loss. Any unrealized losses deemed other-than-temporary are included in current period earnings and removed from accumulated other comprehensive loss.

Investment securities are reviewed for other-than-temporary impairment on a quarterly basis. The determination of other-than-temporary impairment will often depend on several factors, including the severity and duration of the decline in value of the investment securities and the financial condition of the issuer, and requires judgment. To the extent that Merrill Lynch has the ability and intent to hold the investments for a period of time sufficient for a forecasted market price recovery up to or beyond the cost of the investment, no impairment charge will be recognized.

Restricted Investments

Merrill Lynch holds investments that may have quoted market prices but that are subject to restrictions (e.g., requires consent of the issuer or other investors to sell) that may limit Merrill Lynch's ability to realize the quoted market price. Restricted investments may be recorded in either trading assets or investment securities. Merrill Lynch estimates the fair value of these securities taking into account the restrictions, which may result in a fair value for a security that is less than its quoted market price.

Private Equity Investments

Certain private equity investments are held at fair value. Private equity investments that have defined exit strategies and are held for capital appreciation and/or current income are accounted for under the AICPA Accounting and Auditing Guide, *Investment Companies* ("Investment Company Guide") and carried at fair value. Investments are initially carried at original cost, and are adjusted when changes in the underlying fair values are readily ascertainable, generally based on specific events (for example recapitalizations and initial public offerings ("IPOs")), or expected cash flows and market comparables of similar companies.

Loans and Allowance for Loan Losses

Certain loans held by Merrill Lynch are carried at fair value or lower of cost or market ("LOCOM"), and estimation is required in determining these fair values. The fair value of loans made in connection with commercial lending activity, consisting primarily of senior debt, is primarily estimated using discounted cash flows or the market value of publicly issued debt instruments. Merrill Lynch's estimate of fair value for other loans, notes, and mortgages is determined based on the individual loan characteristics. For certain homogeneous categories of loans, including residential mortgages and home equity loans, fair value is estimated using market price quotations or previously executed transactions for securities backed by similar loans, adjusted for credit risk and other individual loan characteristics. For Merrill Lynch's variable-rate loan receivables, carrying value approximates fair value.

Loans held for investment are carried at cost, less a provision for loan losses. This provision for loan losses is based on management's estimate of the amount necessary to maintain the allowance at a level adequate to absorb probable incurred loan losses. Management's estimate of loan losses is influenced by many factors, including adverse situations that may affect the borrower's ability to repay, current economic conditions, prior loan loss experience, and the estimated fair value of any underlying collateral. The fair value of collateral is generally determined by third-party appraisals in the case of residential mortgages or quoted market prices for securities, or estimates of fair value for other assets. Management's estimates of loan losses include considerable judgment about collectibility based on available facts and evidence at the balance sheet date, and the uncertainties inherent in those assumptions. While management uses the best information available on which to base its estimates, future adjustments to the allowance may be necessary based on changes in the economic environment or variances between actual results and the original assumptions used by management.

Legal and Other Reserves

Merrill Lynch is a party in various actions, some of which involve claims for substantial amounts. Amounts are accrued for the financial resolution of claims that have either been asserted or are deemed probable of assertion if, in the opinion of management, it is both probable that a liability has been incurred and the amount of the liability can be reasonably estimated. In many cases, it is not possible to determine whether a liability has been incurred or to estimate the ultimate or minimum amount of that liability until years after the litigation has been commenced, in which case no accrual is made until that time. Accruals are subject to significant estimation by management with input from outside counsel.

Income Taxes

Merrill Lynch provides for income taxes on all transactions that have been recognized in the Consolidated Financial Statements in accordance with SFAS No. 109 *Accounting for Income Taxes.* Accordingly, deferred taxes are adjusted to reflect the tax rates at which future taxable amounts will likely be settled or realized. The effects of tax rate changes on future deferred tax liabilities and deferred tax assets, as well as other changes in income tax laws, are recognized in net earnings in the period during which such changes are enacted. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized. Merrill Lynch assesses its ability to realize deferred tax assets primarily based on the earnings history and future earnings potential of the legal entities through which the deferred tax assets will be realized as discussed in SFAS No. 109, *Accounting for Income Taxes.* See Note 15 to the Consolidated Financial Statements for further discussion of income taxes.

ML & Co. and certain of its wholly-owned subsidiaries file a consolidated U.S. federal income tax return. Certain other Merrill Lynch entities file tax returns in their local jurisdictions.

Variable Interest Entities

In the normal course of business, Merrill Lynch enters into a variety of transactions with VIEs. The applicable accounting guidance requires Merrill Lynch to perform a qualitative and/or quantitative analysis of a VIE to determine whether it is the primary beneficiary of the VIE and therefore must consolidate the VIE. In performing this analysis, Merrill Lynch makes assumptions regarding future performance of assets held by the VIE, taking into account estimates of credit risk, estimates of the fair value of assets, timing of cash flows, and other significant factors. It should also be noted that although a VIE's actual results may differ from projected outcomes, a revised consolidation analysis is not required. If a VIE meets the conditions to be considered a QSPE, it is not required to be consolidated by Merrill Lynch. A QSPE's activities must be significantly limited. A servicer of the assets held by a QSPE may have discretion in restructuring or working out assets held by the QSPE as long as the discretion is significantly limited and the parameters of that discretion are fully described in the legal documents that established the QSPE. Determining whether the activities of a QSPE and its servicer meet these conditions requires the use of judgment by management.

Goodwill and Other Intangibles

Merrill Lynch makes certain subjective and complex judgments with respect to its goodwill and other intangible assets. These include assumptions and estimates used to determine the fair value of its reporting units. Reporting unit fair value is measured based on the market approach, using market-multiple analyses. Merrill Lynch also makes assumptions and estimates in valuing its intangible assets and determining the useful lives of its intangible assets with definite lives.

Employee Stock Options

The fair value of stock options is estimated as of the grant date based on a Black-Scholes option pricing model. The Black-Scholes model takes into account the exercise price and expected life of the option, the current price of the underlying stock and its expected volatility, expected dividends, and the risk-free interest rate for the expected term of the option. Judgment is required in determining certain of the inputs to the model. The expected life of the option is based on an analysis of historical employee exercise behavior. The expected volatility is based on Merrill Lynch's historical monthly stock price volatility for the same number of months as the expected life of the option. The fair value of the option estimated at grant date is not adjusted for subsequent changes in assumptions.

Insurance Reserves and Deferred Acquisition Costs Relating to Insurance Policies

Merrill Lynch records reserves related to life insurance and annuity contracts. Included in these reserves is a mortality reserve that is determined by projecting expected guaranteed benefits under multiple scenarios. Merrill Lynch uses estimates for mortality and surrender assumptions based on actual and projected experience for each contract type. These estimates are consistent with the estimates used in the calculation of deferred policy acquisition costs.

Merrill Lynch records deferred policy acquisition costs that are amortized in proportion to the estimated future gross profits for each group of contracts over the anticipated life of the insurance contracts, utilizing an effective yield methodology. These future gross profit estimates are subject to periodic evaluation by Merrill Lynch, with necessary revisions applied against amortization to date.

Fair Value

At December 29, 2006, $774 billion, or 92%, of Merrill Lynch's total assets and $775 billion, or 97%, of Merrill Lynch's total liabilities were carried at fair value or at amounts that approximate fair value. At December 30, 2005, $613 billion, or 90%, of Merrill Lynch's total assets and $622 billion, or 96%, of Merrill Lynch's total liabilities were carried at fair value or at amounts that approximate such values. Financial instruments that are carried at fair value include cash and cash equivalents, cash and securities segregated for regulatory purposes or deposited with clearing organizations, trading assets and liabilities, securities received as collateral and obligations to return securities received as collateral, available-for-sale and trading securities included in investment securities, certain private equity investments, certain investments of insurance subsidiaries and certain other investments.

Financial instruments recorded at amounts that approximate fair value include receivables under resale agreements, receivables under securities borrowed transactions, other receivables, payables under repurchase agreements, payables under securities loaned transactions, commercial paper and other short-term borrowings, deposits, other payables, and certain long-term borrowings. The fair value of these items is not materially sensitive to shifts in market interest rates because of the short-term nature of many of these instruments and/or their variable interest rates.

The fair value amounts for financial instruments are disclosed in each respective Note to the Consolidated Financial Statements.

Revenue Recognition

Principal transactions revenues include both realized and unrealized gains and losses on trading assets and trading liabilities and investment securities classified as trading investments. Realized gains and losses are recognized on a trade date basis.

Managed accounts and other fee-based revenues primarily consist of asset-priced portfolio service fees earned from the administration of separately managed and other investment accounts for retail investors, annual account fees, and certain other account-related fees.

In addition, until the BlackRock merger at the end of the third quarter of 2006, managed accounts and other fee-based revenues also included fees earned from the management and administration of retail mutual funds and institutional funds such as pension assets, and performance fees earned on certain separately managed accounts and institutional money management arrangements.

Commissions revenues includes commissions, mutual fund distribution fees and contingent deferred sales charge revenue, which are all accrued as earned. Commissions revenues also includes mutual fund redemption fees, which are recognized at the time of redemption. Commissions revenues earned from certain customer equity transactions are recorded net of related brokerage, clearing and exchange fees.

Investment banking revenues include underwriting revenues and fees for merger and acquisition advisory services, which are accrued when services for the transactions are substantially completed. Transaction-related expenses are deferred to match revenue recognition. Investment banking and advisory services revenues are presented net of transaction-related expenses.

Revenues from consolidated investments and expenses of consolidated investments are related to investments that are consolidated under SFAS No. 94 and FIN 46R. Expenses of consolidated investments primarily consist of minority interest expense and are part of Merrill Lynch's private equity and principal investment activities.

Other revenues include fair value adjustments to Merrill Lynch's private equity investments, earnings from investments accounted for using the equity method and other miscellaneous revenues.

Balance Sheet Captions

The following are descriptions of specific balance sheet captions. Refer to the related Notes to the Consolidated Financial Statements for additional information.

Cash and Cash Equivalents

Merrill Lynch defines cash equivalents as short-term, highly liquid securities, federal funds sold, and interest-earning deposits with maturities, when purchased, of 90 days or less, that are not used for trading purposes.

Cash and Securities Segregated for Regulatory Purposes or Deposited with Clearing Organizations

Merrill Lynch maintains relationships with clients around the world and, as a result, it is subject to various regulatory regimes. As a result of its client activities, Merrill Lynch is obligated by rules mandated by its primary regulators, including the Securities and Exchange Commission ("SEC") and the Commodities Futures Trading Commission ("CFTC") in the United States and the Financial Services Authority ("FSA") in the United Kingdom to segregate or set aside cash and/or qualified securities to satisfy these regulations, which have been promulgated to protect customer assets. In addition, Merrill Lynch is a member of various clearing organizations at which it maintains cash and/or securities required for the conduct of its day-to-day clearance activities.

Securities Financing Transactions

Merrill Lynch enters into repurchase and resale agreements and securities borrowed and loaned transactions to accommodate customers (also referred to as "matched-book transactions"), and earn residual interest rate spreads, obtain securities for settlement and finance inventory positions. Merrill Lynch also engages in securities financing for customers through margin lending (see the customer receivables and payables section).

Resale and repurchase agreements are accounted for as collateralized financing transactions and are recorded at their contractual amounts plus accrued interest. Merrill Lynch's policy is to obtain possession of collateral with a market value equal to or in excess of the principal amount loaned under resale agreements. To ensure that the market value of the underlying collateral remains sufficient, collateral is valued daily, and Merrill Lynch may require counterparties to deposit additional collateral or return collateral pledged, when appropriate.

Substantially all repurchase and resale activities are transacted under master netting agreements that give Merrill Lynch the right, in the event of default, to liquidate collateral held and to offset receivables and payables with the same counterparty. Merrill Lynch offsets certain repurchase and resale agreement balances with the same counterparty on the Consolidated Balance Sheets.

Merrill Lynch may use securities received as collateral for resale agreements to satisfy regulatory requirements such as Rule 15c3-3 of the SEC.

Securities borrowed and loaned transactions are recorded at the amount of cash collateral advanced or received. Securities borrowed transactions require Merrill Lynch to provide the counterparty with collateral in the form of cash, letters of credit, or other securities. Merrill Lynch receives collateral in the form of cash or other securities for securities loaned transactions. For these transactions, the fees received or paid by Merrill Lynch are recorded as interest revenue or expense. On a daily basis, Merrill Lynch monitors the market value of securities borrowed or loaned against the collateral value, and Merrill Lynch may require counterparties to deposit additional collateral or return collateral pledged, when appropriate.

All firm-owned securities pledged to counterparties where the counterparty has the right, by contract or custom, to sell or repledge the securities are disclosed parenthetically in trading assets and investment securities on the Consolidated Balance Sheets.

In transactions where Merrill Lynch acts as the lender in a securities lending agreement and receives securities that can be pledged or sold as collateral, it recognizes an asset on the Consolidated Balance Sheets, representing the securities received (securities received as collateral), and a liability for the same amount, representing the obligation to return those securities (obligation to return securities received as collateral). The amounts on the Consolidated Balance Sheets result from non-cash transactions.

Trading Assets and Liabilities

Merrill Lynch's trading activities consist primarily of securities brokerage and trading; derivatives dealing and brokerage; commodities trading and brokerage; and securities financing transactions. Trading assets and trading liabilities consist of cash instruments (such as securities and loans) and derivative instruments used for trading purposes or for managing risk exposures in other trading inventory. See the Derivatives section for additional information on accounting policy for derivatives. Trading assets and trading liabilities also include commodities inventory.

Trading securities and other cash instruments (e.g., loans held for trading purposes) are recorded on a trade date basis at fair value. Included in trading liabilities are securities that Merrill Lynch has sold but did not own and will therefore be obligated to purchase at a future date ("short sales"). Commodities inventory is recorded at the lower of cost or market value. Changes in fair value of trading assets and liabilities (i.e., unrealized gains and losses) are recognized as principal transactions revenues in the current period. Realized gains and losses and any related interest amounts are included in principal transactions revenues and interest revenues and expenses, depending on the nature of the instrument.

Fair values of trading assets and liabilities are based on quoted market prices, pricing models (utilizing indicators of general market conditions or other economic measurements), or management's best estimates of amounts to be realized on settlement, assuming current market conditions and an orderly disposition over a reasonable period of time. As previously noted, estimating the fair value of certain trading assets and liabilities requires significant management judgment.

Derivatives

A derivative is an instrument whose value is derived from an underlying instrument or index such as a future, forward, swap, or option contract, or other financial instrument with similar characteristics. Derivative contracts often involve future commitments to exchange interest payment streams or currencies based on a notional or contractual amount (e.g., interest rate swaps or currency forwards) or to purchase or sell other financial instruments at specified terms on a specified date (e.g., options to buy or sell securities or currencies). Derivative activity is subject to Merrill Lynch's overall risk management policies and procedures. See Note 6 to the Consolidated Financial Statements for further information.

Accounting for Derivatives and Hedging Activities

SFAS No. 133, *Accounting for Derivatives and Hedging Activities*, as amended, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts ("embedded derivatives") and for hedging activities. SFAS No. 133 requires that an entity recognize all derivatives as either assets or liabilities in the Consolidated Balance Sheets and measure those instruments at fair value. The fair value of all derivatives is recorded on a net-by-counterparty basis on the Consolidated Balance Sheets where management believes a legal right of setoff exists under an enforceable netting agreement.

The accounting for changes in fair value of a derivative instrument depends on its intended use and if it is designated and qualifies as an accounting hedging instrument.

Merrill Lynch enters into derivatives to facilitate client transactions, for proprietary trading and financing purposes, and to manage its risk exposures arising from trading assets and liabilities. Derivatives entered into for these purposes are recognized at fair value on the Consolidated Balance Sheets as trading assets and liabilities in contractual agreements and the change in fair value is reported in current period earnings as principal transactions revenues.

Merrill Lynch also enters into derivatives in order to manage its risk exposures arising from assets and liabilities not carried at fair value as follows:

1. Merrill Lynch routinely issues debt in a variety of maturities and currencies to achieve the lowest cost financing possible. In addition, Merrill Lynch's regulated bank entities accept time deposits of varying rates and maturities. Merrill Lynch enters into derivative transactions to hedge these liabilities. Derivatives used most frequently include swap agreements that:
   - Convert fixed-rate interest payments into variable payments
   - Change the underlying interest rate basis or reset frequency
   - Change the settlement currency of a debt instrument.
2. Merrill Lynch enters into hedges on marketable investment securities to manage the interest rate risk, currency risk, and net duration of its investment portfolios.
3. Merrill Lynch enters into fair value hedges of long-term fixed rate resale and repurchase agreements to manage the interest rate risk of these assets and liabilities.

4. Merrill Lynch uses foreign-exchange forward contracts, foreign-exchange options, currency swaps, and foreign-currency-denominated debt to hedge its net investments in foreign operations. These derivatives and cash instruments are used to mitigate the impact of changes in exchange rates.
5. Merrill Lynch enters into futures and forwards to manage the price risk of certain commodity inventory.

Derivatives entered into by Merrill Lynch to hedge its funding, marketable investment securities and net investments in foreign subsidiaries are reported at fair value in other assets or interest and other payables on the Consolidated Balance Sheets. Derivatives used to hedge commodity inventory are included in trading assets and trading liabilities on the Consolidated Balance Sheets.

Derivatives that qualify as accounting hedges under the guidance in SFAS No. 133 are designated, on the date they are entered into, as one of the following:

1. A hedge of the fair value of a recognized asset or liability ("fair value" hedge). Changes in the fair value of derivatives that are designated and qualify as fair value hedges of interest rate risk, along with the gain or loss on the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings as interest revenue or expense. Changes in the fair value of derivatives that are designated and qualify as fair value hedges of commodity price risk, along with the gain or loss on the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings in principal transactions.
2. A hedge of the variability of cash flows to be received or paid related to a recognized asset or liability ("cash flow" hedge). Changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recorded in accumulated other comprehensive loss until earnings are affected by the variability of cash flows of the hedged asset or liability (e.g., when periodic interest accruals on a variable-rate asset or liability are recorded in earnings).
3. A hedge of a net investment in a foreign operation. Changes in the fair value of derivatives that are designated and qualify as hedges of a net investment in a foreign operation are recorded in the foreign currency translation adjustment account within accumulated other comprehensive loss. Changes in the fair value of the hedge instruments that are associated with the difference between the spot translation rate and the forward translation rate are recorded in current period earnings in other revenues.

Merrill Lynch formally assesses, both at the inception of the hedge and on an ongoing basis, whether the hedging derivatives are highly effective in offsetting changes in fair value or cash flows of hedged items. When it is determined that a derivative is not highly effective as a hedge, Merrill Lynch discontinues hedge accounting. Under the provisions of SFAS No. 133, 100% hedge effectiveness is assumed for those derivatives whose terms meet the conditions of SFAS No. 133 "short-cut method."

As noted above, Merrill Lynch enters into fair value hedges of interest rate exposure associated with certain investment securities and debt issuances. Merrill Lynch uses interest rate swaps to hedge this exposure. Hedge effectiveness testing is required for certain of these hedging relationships on a quarterly basis. Merrill Lynch assesses effectiveness on a prospective basis by comparing the expected change in the price of the hedge instrument to the expected change in the value of the hedged item under various interest rate shock scenarios. In addition, Merrill Lynch assesses effectiveness on a retrospective basis using the Dollar-Offset ratio approach. When assessing hedge effectiveness, there are no attributes of the derivatives used to hedge the fair value exposure that are excluded from the assessment. In addition, the amount of hedge ineffectiveness on fair value hedges reported in earnings was not material for all periods presented. Merrill Lynch also enters into fair value hedges of commodity price risk associated with certain commodity inventory. For these hedges, Merrill Lynch assesses effectiveness on a prospective and retrospective basis using regression techniques. The difference between the spot rate and the contracted forward rate which represents the time value of money is excluded from the assessment of hedge effectiveness and is recorded in principal transactions. The amount of hedge ineffectiveness on these fair value hedges reported in earnings was not material for all periods presented.

The majority of deferred net gains (losses) on derivative instruments designated as cash flow hedges that were in accumulated other comprehensive loss at December 29, 2006 are expected to be reclassified into earnings over the next three years. The amount of ineffectiveness related to these hedges reported in earnings was not material for all periods presented.

For the years ended 2006 and 2005, respectively, $1.1 billion and $731 million of net losses related to non-U.S. dollar hedges of investments in non-U.S. dollar subsidiaries were included in accumulated other comprehensive loss on the Consolidated Balance Sheets. These amounts were substantially offset by net gains on the hedged investments.

Changes in the fair value of derivatives that are economically used to hedge non-trading assets and liabilities, but that do not meet the criteria in SFAS No. 133 to qualify as an accounting hedge, are reported in current period earnings as either principal transactions revenues, other revenues or expenses, or interest revenues or expenses, depending on the nature of the transaction.

Embedded Derivatives

Merrill Lynch issues debt whose coupons or repayment terms are linked to the performance of debt or equity securities, indices or currencies. The contingent payment components of these obligations may meet the definition in SFAS No. 133 of an "embedded derivative." These debt instruments are assessed to determine if the embedded derivative requires separate reporting and accounting, and if so, the

embedded derivative is accounted for at fair value and reported in long-term borrowings on the Consolidated Balance Sheets along with the debt obligation. Changes in the fair value of the embedded derivative and related economic hedges are reported in principal transactions revenues. Separating an embedded derivative from its host contract requires careful analysis, judgment, and an understanding of the terms and conditions of the instrument.

Merrill Lynch may also purchase financial instruments that contain embedded derivatives. These instruments may be part of either trading inventory or trading marketable investment securities. These instruments are generally accounted for at fair value in their entirety; the embedded derivative is not separately accounted for, and all changes in fair value are reported in principal transactions revenues.

Derivatives that Contain a Significant Financing Element

In the ordinary course of trading activities, Merrill Lynch enters into certain transactions that are documented as derivatives where a significant cash investment is made by one party. These transactions can be in the form of simple interest rate swaps where the fixed leg is prepaid or may be in the form of equity-linked or credit-linked transactions where the initial investment equals the notional amount of the derivative. Certain derivative instruments entered into or modified after June 30, 2003 that contain a significant financing element at inception and where Merrill Lynch is deemed to be the borrower, are included in financing activities in the Consolidated Statements of Cash Flows. Prior to July 1, 2003, the activity associated with such derivative instruments was included in operating activities in the Consolidated Statements of Cash Flows. In addition, the cash flows from all other derivative transactions that do not contain a significant financing element at inception are included in operating activities.

Investment Securities

Investment securities consist of marketable investment securities, investments of Merrill Lynch insurance subsidiaries, and other investments. Refer to Note 5 to the Consolidated Financial Statements for further information.

Marketable Investment Securities

ML & Co. and certain of its non-broker-dealer subsidiaries hold debt and equity investments, which are primarily classified as available-for-sale.

Debt and marketable equity securities classified as available-for-sale are reported at fair value. Unrealized gains or losses on these securities are reported in stockholders' equity as a component of accumulated other comprehensive loss, net of income taxes and other related items. However, to the extent that Merrill Lynch enters into interest rate swaps to hedge the interest rate exposure of certain available-for-sale investment securities, the gain or loss on the derivative instrument, as well as the offsetting loss or gain on the investment security, are recorded in current period earnings as interest revenue or expense (Refer to the Derivatives section for additional information). Any unrealized losses deemed other-than-temporary are included in current period earnings.

Debt securities that Merrill Lynch has the positive intent and ability to hold to maturity are classified as held-to-maturity. These investments are recorded at amortized cost unless a decline in value is deemed other-than-temporary, in which case the carrying value is reduced. The amortization of premiums or accretion of discounts and any unrealized losses deemed other-than-temporary are included in current period earnings.

Debt and marketable equity securities purchased principally for the purpose of resale in the near term are classified as trading investments and are reported at fair value. Unrealized gains or losses on these investments are included in current period earnings.

Realized gains and losses on all investment securities are included in current period earnings. For purposes of computing realized gains and losses, the cost basis of each investment sold is generally based on the average cost method.

Investments of Insurance Subsidiaries and Related Liabilities

Insurance liabilities are future benefits payable under annuity and life insurance contracts and include deposits received plus interest credited during the contract accumulation period, the present value of future payments for contracts that have annuitized, and a mortality provision for certain products. Certain policyholder liabilities are also adjusted for those investments classified as available-for-sale. Liabilities for unpaid claims consist of the mortality benefit for reported claims and an estimate of unreported claims based upon actual and projected experience for each contract type.

Security investments of insurance subsidiaries are classified as available-for-sale and recorded at fair value. These investments support Merrill Lynch's in-force, universal life-type contracts. Merrill Lynch records adjustments to policyholder account balances which equals the gain or loss that would have been recorded if those available-for-sale investments had been sold at their estimated fair values and the proceeds reinvested at current yields. The corresponding credits or charges for these adjustments are recorded in stockholders' equity as a component of accumulated other comprehensive loss, net of applicable income taxes.

Certain variable costs related to the sale or acquisition of new and renewal insurance contracts have been deferred, to the extent deemed recoverable, and amortized over the estimated lives of the contracts in proportion to the estimated gross profit for each group of contracts.

Other Investments

Other investments include private equity investments, which are accounted for at fair value in accordance with the Investment Company Guide.

Merrill Lynch has minority investments in the common shares of corporations and in partnerships that do not fall within the scope of SFAS No. 115 or the Investment Company Guide. Where the investments are strategic in nature, Merrill Lynch will account for the investments using either the cost or the equity method of accounting based on management's ability to influence the investees (See Consolidation Accounting Policies section for more information).

For investments accounted for using the equity method, income is recognized based on Merrill Lynch's share of the earnings (or losses) of the investee. Dividend distributions are recorded as reductions in the investment balance. Impairment testing is based on the guidance provided in FASB Staff Position SFAS No. 115, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* ("FSP SFAS No. 115"), and the investment would be reduced when an impairment is deemed other than temporary.

For investments accounted for at cost, income is recognized as dividends are received. Impairment testing is based on the guidance provided in FSP SFAS No. 115, and the cost basis would be reduced when an impairment is deemed other than temporary.

Other Receivables and Payables

Customer Receivables and Payables

Customer securities transactions are recorded on a settlement date basis. Receivables from and payables to customers include amounts due on cash and margin transactions, including futures contracts transacted on behalf of Merrill Lynch customers. Securities owned by customers, including those that collateralize margin or other similar transactions, are not reflected on the Consolidated Balance Sheets.

Brokers and Dealers Receivables and Payables

Receivables from brokers and dealers include amounts receivable for securities not delivered by Merrill Lynch to a purchaser by the settlement date ("fails to deliver"), margin deposits, commissions, and net receivables arising from unsettled trades. Payables to brokers and dealers include amounts payable for securities not received by Merrill Lynch from a seller by the settlement date ("fails to receive"). Brokers and dealers receivables and payables also include amounts related to futures contracts on behalf of Merrill Lynch customers as well as net payables and receivables from unsettled trades.

Interest and Other Receivables and Payables

Interest and other receivables include interest receivable on corporate and governmental obligations, customer or other receivables, and stock-borrowed transactions. Also included are receivables from income taxes, underwriting and advisory fees, commissions and fees, and other receivables. Interest and other payables include interest payable for stock-loaned transactions, and short-term and long-term borrowings. Also included are amounts payable for employee compensation and benefits, income taxes, minority interest, non-trading derivatives, dividends, other reserves, and other payables.

Loans, Notes, and Mortgages, Net

Merrill Lynch's lending and related activities include loan originations, syndications, and securitizations. Loan originations include corporate and institutional loans, residential and commercial mortgages, asset-based loans, and other loans to individuals and businesses. Merrill Lynch also engages in secondary market loan trading and margin lending (see trading assets and liabilities and customer receivables and payables sections, respectively). Loans included in loans, notes, and mortgages are classified for accounting purposes as loans held for investment and loans held for sale.

Loans held for investment purposes include:

- commercial loans (includes small- and middle-market business loans);
- certain consumer loans; and
- certain residential mortgage loans.

These loans are carried at their principal amount outstanding. An allowance for loan losses is established through provisions that are based on management's estimate of probable incurred losses. Loans are charged off against the allowance for loan losses when management determines that the loan is uncollectible. The loan loss provision related to loans held for investment is included in interest revenue in the Consolidated Statements of Earnings. In general, loans are evaluated for impairment when they are greater than 90 days past due or exhibit credit quality weakness. Loans are considered impaired when it is probable that Merrill Lynch will not be able to collect the contractual principal and interest due from the borrower. All payments received on impaired loans are applied to principal until the principal

balance has been reduced to a level where collection of the remaining recorded investment is not in doubt. Typically, when collection of principal on an impaired loan is not in doubt, contractual interest will be credited to interest income when received.

Loans held for sale include:

- commercial loans that are in the process of being syndicated;
- certain purchased automobile loans; and
- certain residential mortgage loans which are typically sold via securitization.

These loans are reported at LOCOM. Declines in the carrying value of loans held for sale are included in other revenues in the Consolidated Statements of Earnings.

Nonrefundable loan origination fees, loan commitment fees, and "draw down" fees received in conjunction with financing arrangements are generally deferred and recognized over the contractual life of the loan as an adjustment to the yield. If, at the outset, or any time during the term of the loan, it becomes highly probable that the repayment period will be extended, the amortization is recalculated using the expected remaining life of the loan. When the loan contract does not provide for a specific maturity date, management's best estimate of the repayment period is used. At repayment of the loan, any unrecognized deferred fee is immediately recognized in earnings.

Separate Accounts Assets and Liabilities

Merrill Lynch maintains separate accounts representing segregated funds held for purposes of funding variable life and annuity contracts. The separate accounts assets are not subject to general claims of Merrill Lynch. These accounts and the related liabilities are recorded as separate accounts assets and separate accounts liabilities on the Consolidated Balance Sheets.

Absent any contract provision wherein Merrill Lynch guarantees either a minimum return or account value upon death or annuitization, the net investment income and net realized and unrealized gains and losses attributable to separate accounts assets supporting variable life and annuity contracts accrue directly to the contract owner and are not reported as revenue in the Consolidated Statements of Earnings. Mortality, policy administration and withdrawal charges associated with separate accounts products are included in other revenues in the Consolidated Statements of Earnings.

Equipment and Facilities

Equipment and facilities consist primarily of technology hardware and software, leasehold improvements, and owned facilities. Equipment and facilities are reported at historical cost, net of accumulated depreciation and amortization, except for land, which is reported at historical cost.

Depreciation and amortization are computed using the straight-line method. Equipment is depreciated over its estimated useful life, while leasehold improvements are amortized over the lesser of the improvement's estimated economic useful life or the term of the lease. Maintenance and repair costs are expensed as incurred.

Included in the occupancy and related depreciation expense category was depreciation and amortization of $219 million, $200 million, and $198 million in 2006, 2005, and 2004, respectively. Depreciation and amortization recognized in the communications and technology expense category was $304 million, $273 million, and $308 million for 2006, 2005, and 2004, respectively.

Qualifying costs incurred in the development of internal-use software are capitalized when costs exceed $5 million and are amortized over the useful life of the developed software, generally not exceeding three years.

Goodwill

Goodwill is tested annually (or more frequently under certain conditions) for impairment in accordance with SFAS 142, *"Goodwill and Other Intangible Assets"*. Merrill Lynch has reviewed its goodwill and determined that there was no impairment related to any period presented.

Goodwill at December 29, 2006 was $2,209 million compared to $5,803 million at December 30, 2005. The majority of the goodwill balance at December 29, 2006 and December 30, 2005, related to the Global Markets and Investment Banking ("GMI") business and the Merrill Lynch Investment Managers ("MLIM") business, respectively. The decrease in goodwill during 2006 was primarily due to the merger of the MLIM business with BlackRock for which goodwill associated with the MLIM business was derecognized. The decrease in goodwill was partially offset by an increase in the ownership of a joint venture related to the GMI business segment and other acquisitions.

Goodwill at December 30, 2005 was $5,803 million compared to $6,035 million at December 31, 2004. The majority of the goodwill balance at December 30, 2005 and December 31, 2004 related to the MLIM business. The decrease in goodwill during 2005 was primarily due to the translation impact of changes in foreign exchange rates. The decrease was partially offset by an increase in goodwill related to the acquisition of The Advest Group, Inc. ("Advest") within the Global Wealth Management ("GWM") segment.